

Office Market Trends Sacramento

Grubb & Ellis Research

First Quarter 2006



New Supply Weighing In

Executive Summary

Net absorption dipped into negative territory for the first time in over a year, dragging vacancy up to just over 16 percent. Vacating tenants and vacant new construction completions both contributed to the increase. Average asking rates remained virtually the same at \$2.15 and \$1.85 per square foot full service for Class A and B properties, respectively, across all submarkets.

Local unemployment was a very healthy 4.8 percent at the end of February. While this figure does mark a slight increase over January, it is significantly lower than the 5.4 percent predicted by analysts last year and is still indicative of a very healthy local economy. Virtually all employment sectors posted increases in paid positions during the quarter. Restaurants, professional and business services, health and social services and financial services all noted increases in the month of February. Further, construction, which had been posting primarily seasonal decreases since November, also posted an increase in jobs during February, boding well for a local mainstay. At 4.1 percent, Placer County has the lowest unemployment rate in the four-county Sacramento MSA. The State and federal unemployment rates were 5.4 percent and 5.1 percent, respectively, for this same period.

Contents

Executive Summary	1
Market Assessment	2
Forecast	3
Opportunities & Challenges . .	3
Market Snapshot	4

Sacramento Office Market Trends

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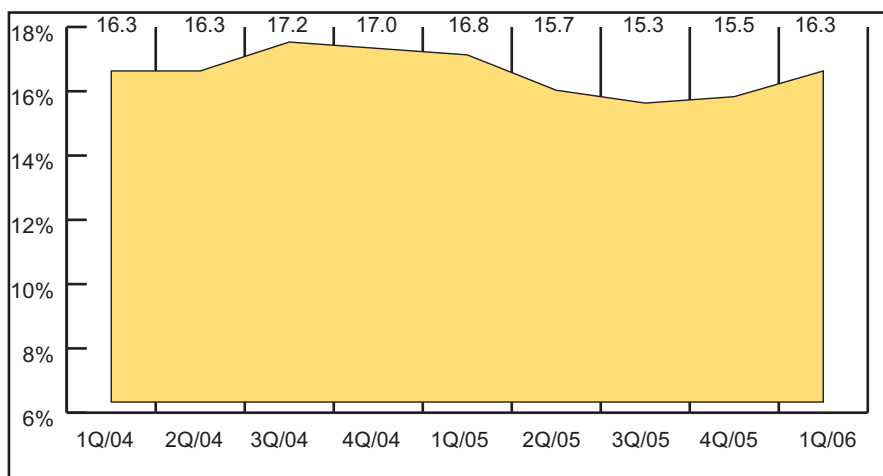
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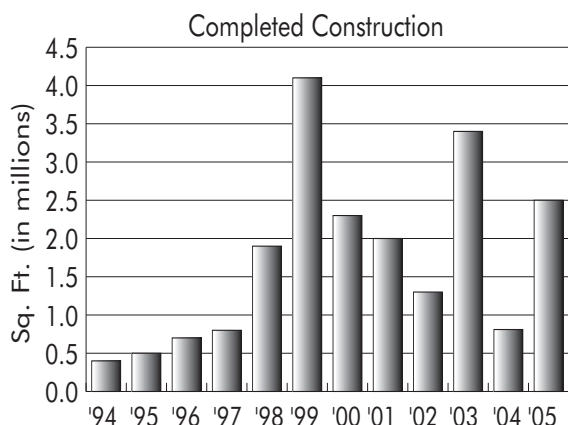
Office Vacancy Rate*

* All Classes of Space

Office Market Trends First Quarter 2006

Market Assessment

While up slightly over the end of 2005, vacancy rates are not expected to trend up significantly during the remainder of the year. One factor contributing to the current increase in vacancy that will be not present in the coming months is the first quarter timing of statistical adjustments to the competitive inventory. While minimal in individual focus, in totality, these adjustments to building size and vacancy can have a measurable impact market-wide. Also, several significantly preleased buildings that were "completed" during the first quarter have not yet been occupied. In these cases, it is not until the completion of tenant improvements and actual occupancy that positive net absorption will be realized. New construction in the relatively smaller submarkets of Folsom and Elk Grove stand to be significantly affected by this phenomenon due to the proportional weight a new project bears relative to the overall submarket size.



The Downtown submarket endured the greatest loss in occupied space during the quarter. The State of California vacated 200,000 square feet at 400 R Street for the new publicly-owned facility on Q Street. As the new CalPers site is not part of the competitive CBD inventory, this tenant has effectively left the marketplace. As a result of this move, Class B vacancy in the Downtown submarket now exceeds 20 percent.

Roseville/Rocklin continued to lead the numbers in positive net absorption during the first quarter. The single largest net absorption figure for any building in the market was EOP's Summit at Douglas Ridge, located at 3741 Douglas Boulevard in Roseville. This building completed during the third quarter of 2005 and now 65 percent occupied is exemplary of the process by which a newly completed building undergoing tenant improvements may take up to a year to become occupied. Including the several new projects completed during the quarter, Class A vacancy in Roseville is now 14.3

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Office Market Trends First Quarter 2006

percent. This number is expected to decrease to under 11 percent over the next 90 days as a number of tenants who preleased space in this very popular submarket take possession of their spaces.

Forecast

The skeleton of 621 Capitol will begin to take shape in the CBD skyline in 2006. Site work has commenced on David Taylor's new project and it's anticipated that this building will go vertical within the next 120 days.

While the affinity for ownership is still strong, the impact of multiple interest rate hikes has re-energized the leasing market. The same submarkets will continue the performance trends established in 2005 in 2006. Look for Roseville/Rocklin to again post significant net absorption figures during the year. Douglas Boulevard and the adjacent neighborhood will continue to be the hot spot in that submarket. There will be significant growth in the newer suburban submarkets in 2006. With a cumulative total of just over one million square feet of speculative projects underway, the Folsom/El Dorado Hills, Laguna/Elk Grove and Roseville/Rocklin submarkets will add 10 percent to their Class A inventories during the year.

The investment market, having experienced some cooling over the last quarter will see a gradual return to more realistic capitalization rates. As the local investment feeding frenzy wanes, cap rates will rise, most likely settling in the mid-to high 7 percent range.

Opportunities and Challenges

The 170 new tenant requirements noted during the first quarter definitely present the single greatest source of opportunity for growth in the office market in the coming months. At 1.4 million square feet, this figure is the strongest first quarter reading in the last three years. Further, at just under 9,000 square feet, the average size tenant in the marketplace right now offers the prospect of absorbing more space more quickly than in the last several years.

Major Transactions

Grubb & Ellis is pleased to announce that we represented the following companies in office transactions during the fourth quarter of 2005:

Foothill Corp. Center

26,024 square foot lease
to CEMEX, Inc.
El Dorado Hills, CA
Tom Walcott, SIOR

Touchstone Investments

\$27,000,000 investment sale
Creekside Portfolio
Heath Charamuga, Erik Neese,
Susanne Baker, Patrick Ronan,
Kye Huff

Pick-N-Pull Auto Dismantlers

14,324 square foot lease
10850 Gold Center Drive
Rancho Cordova, CA
Clyde Rawlings

Office Market Terms and Definitions

Inventory: Office inventory includes all multi-tenant and single tenant buildings at least 10,000 square feet. Owner-occupied, government and medical buildings are not included.

Construction Type: Speculative ("spec") construction is designed to attract tenants likely to be in the market when the project is leasing. Build-to-suit construction is designed for a specific tenant.

Office Building Classifications: Grubb & Ellis adheres to the BOMA guidelines. Class A properties are the most prestigious buildings competing for premier office users with rents above average for the area. Class B properties compete for a wide range of users with rents in the average range for the area. Class C buildings compete for tenants requiring functional space at rents below the area average.

Vacancy and Availability: The vacancy rate is the amount of physically vacant space divided by the inventory. The availability rate is the amount of space available for lease divided by the inventory.

Net Absorption: The net change in physically occupied space over a period of time.

Asking Rent: The dollar amount asked by landlords for available space expressed in dollars per square foot per month. Office rents are reported as full service where all costs of operation are paid by the landlord up to a base year or expense stop.

Average Weighted Asking Rent: An average market rent where the asking rent for each building in the market is weighted by the building size.

Office Market Snapshot Sacramento First Quarter 2006

By Submarket (All Classes)	Total SF(1)	Vacant SF (2)	Vacant %	Net Absorption		Under Construction(3)	Asking Rent(4)	
				Current Qtr.	Year-to-date		Class A	Class B
CBD (Downtown)	9,521,958	1,533,664	16.1%	(257,848)	(257,848)	330,000	\$2.65	\$1.84
Carm/F.O./C.H./O'Vale	1,206,100	69,839	5.8%	(8,202)	(8,202)	-	-	\$1.57
Folsom/El Do. Hills	3,225,810	561,602	17.4%	63,294	63,294	264,892	\$2.05	\$1.91
Highway 50	12,187,800	2,051,741	16.8%	(40,435)	(40,435)	-	\$1.63	\$1.55
Highway 80	5,802,431	694,408	12.0%	(22,080)	(22,080)	27,750	\$2.04	\$1.66
Laguna/Elk Grove	462,470	131,013	28.3%	(2,341)	(2,341)	211,486	\$2.30	\$2.71
Midtown	2,202,584	248,806	11.3%	2,025	2,025	-	\$1.75	\$1.61
Natomas	5,481,406	996,372	18.2%	23,747	23,747	293,905	\$1.99	\$1.71
North Sacramento	1,538,077	602,377	39.2%	741	741	120,000	\$1.55	\$1.34
Roseville/Rocklin	6,156,324	809,778	13.2%	165,474	165,474	572,670	\$2.23	\$1.93
South Sacramento	947,447	141,184	14.9%	19,551	19,551	-	-	\$1.58
West Sacramento	1,434,496	357,730	24.9%	9,418	9,418	-	\$1.55	\$1.47
CBD	9,521,958	1,533,664	16.1%	(257,848)	(257,848)	330,000	\$2.65	\$1.84
Suburban	40,644,945	6,664,850	16.4%	211,192	211,192	1,490,703	\$1.90	\$1.67
Total	50,166,903	8,198,514	16.3%	(46,656)	(46,656)	1,820,703	\$2.12	\$1.70
By Class (All Submarkets)							Available for Sublease	
							CBD	Suburban
Class A	24,638,329	3,820,737	15.5%	(32,339)	(32,339)	1,188,600	66,942	444,589
Class B	18,227,509	3,245,259	17.8%	(19,312)	(19,312)	632,103	14,793	151,259
Class C	7,301,065	1,132,518	15.5%	4,995	4,995	-	9,767	31,276
Total	50,166,903	8,198,514	16.3%	(46,656)	(46,656)	1,820,703	91,502	627,124

(1) Inventory includes multi-tenant and single tenant buildings with at least 10,000 sq. ft.

(2) Vacant space includes both vacant direct and vacant sublease space.

(3) Space under construction includes speculative and build-to-suit for lease projects.

(4) Asking rates are per square foot per month full service. Rates for each building are weighted by the size of the building.

* Grubb & Ellis statistics are audited annually and may result in revisions to previously reported quarterly and final year-end figures.